Chambre de commerce
du Montréal métropolitain
Board of Trade of Metropolitan Montreal

Federal Pre-Budget Submission 2004-2005

"Investing in Canada's Innovation, Productivity and Competitiveness"

Presented to

The Honourable Ralph E. Goodale

Minister of Finance

by the

Board of Trade of Metropolitan Montreal

January 2004

Table of contents

Chambre de commerce
du Montréal métropolitain
Board of Trade of Metropolitan Montreal

Summary of recommendations

Improving city financing

The Board of Trade recommends:

- That the Government of Canada work closely with the provincial governments and representatives of Canadian cities to find ways of increasing and diversifying the revenue sources of cities. The reflection in this regard should begin during this fiscal year and lead to profound, lasting changes in city financing by no later than the 2005-2006 budget.

- That the Government of Canada share a portion of the gasoline excise tax revenues with the large cities in the country.

- That as of the next budget year, the Government of Canada exempt municipalities from GST or fully refund them the tax.

- That the compensation in lieu of taxes paid by the Government of Canada and its Crown corporations to the municipalities equal 100% of the local taxes on the property value of all the buildings they own, as of the next budget year.

Enhancing our economic competitiveness

The Board of Trade recommends:

- That the governments of Quebec and Canada, in conjunction with municipal administrations, jointly and actively participate in setting up "public works, private capital" partnerships to finance value-added urban infrastructures.

- That the Government of Canada immediately and completely abolish the large corporations tax, or federal capital tax, a tax measure considered to be highly detrimental to business productivity.

- That the Government of Canada set up export support measures such as a government-backed fund devoted exclusively to financing the export projects of low- and medium-technology companies.

The Board of Trade of Metropolitan Montreal has some 7,000 members. Its primary mission is to represent the interests of the business community of the Greater Montreal region and, as a contributing and responsible player, to promote the economic development of the urban area. Encompassing three specialized services (Info entreprises, the Electronic Commerce Institute and World Trade Centre Montréal) that serve merchants and businesses of all sizes throughout Quebec and Canada, the Board of Trade is Quebec's leading private economic development organization.

Introduction

Once again this year, the Board of Trade of Metropolitan Montreal would like to take advantage of the pre-budget consultation period to present the expectations of its members to the government along with a series of concrete recommendations. The theme "innovation-productivity-competitiveness" underpinned the Board of Trade's pre-budget reflection, and the recommendations revolve around the need to invest in the innovation, productivity and competitiveness Canada.

From an economic perspective, 2003 was not a very good year for Greater Montreal, which was plagued by anaemic growth and job losses for a good part of that period. The meteoric rise of the Canadian dollar was a major headache for Canadian and Quebec exporters, 70% of which are located in Greater Montreal, while SARS kept tourists away from major cities, including Montreal. Then there was the uncertainty surrounding the future of the two new cities of the metropolitan region – Montreal and Longueuil – following the Quebec government's adoption in December of Bill 9 allowing the consultation of citizens on the creation of new cities. Given that Montreal is already lagging far behind its North American counterparts in terms of per capita GDP (26th out of 26), 2003 was a year that, economically speaking, Montreal could have done without.

While the outlook for 2004 is better – the job situation in Montreal is improving and the economic recovery in the U.S. appears to be more assured – it is still important that the next budget pay special attention to Canada's ability to create more wealth for its citizens.

In this pre-budget submission, the Board of Trade first puts forward its main expectations regarding the guiding principles that should shape the next budget. It then sets out, in greater detail, specific recommendations in keeping with these expectations. These recommendations are grouped under two themes: 1) improving city financing, and 2) boosting Canada's economic competitiveness. Insofar as Canada's large cities are the country's economic engines, the Board of Trade believes that a government interested in investing in the innovation, productivity and competitiveness of our economy must take concrete, parallel actions on all these fronts.

I. The Board of Trade's expectations

a) A rigorously balanced budget

The Board of Trade expects the next **budget to be balanced.** The government must act responsibly in its budget management. A return to a deficit during times of economic growth is neither desirable nor justified. As well, the Board of Trade expects the government to demonstrate exemplary **rigour and transparency** in its management of the public purse. If the population is to continue having faith in the government's ability to manage its finances, the government must present a budget with no accounting acrobatics and obscure technical changes that nonetheless impact on the wallet of Canadians. Moreover, the Board of Trade believes that economic growth forecasts should be conservative, and in this regard supports the idea that the budget provide for a reserve fund.

b) Recognize the key role of urban centres and their businesses

For the Board of Trade, it is paramount that in its next budget the government finally recognize the key role urban centres and their businesses play in the economic growth of the country. This recognition should translate into concrete measures to make both SMEs and large businesses more competitive and decisions that allow large cities to more effectively assume a catalyst role in economic development. Among these measures, providing cities with access to new, predictable, recurring and diversified revenue sources should be a priority.

c) Invest in Canada's innovation, productivity and competitiveness

While the Board of Trade believes the government must limit its spending increases, it does support making strategic investments that will boost the innovativeness, productivity and competitiveness of the Canadian economy. For the Board of Trade, a **controlled increase in spending** could be appropriate in certain strategic sectors. The areas in which the Board of Trade would support such investments are as follows:

- City financing – namely, by providing access to new, predictable, recurring and diversified revenue sources for cities, thereby allowing them to shift away from financial dependence on the upper levels of government towards a greater capacity for economic development;

- Infrastructures – namely, by completing the construction of Greater Montreal's highway network and rehabilitating existing urban infrastructures such as the metro and water supply system;

d) Towards reducing the tax burden

The Board of Trade considers it pertinent for the Canadian government to contemplate measures to reduce the tax burden of Canadians. The fiscal environment is an important element of competitiveness, and our tax system competes with that of other countries for workers and companies alike. The Board of Trade therefore supports measures aimed at reducing the tax burden, provided however, that such measures do not thwart the achievement of the other previously mentioned principles and objectives. As well, the Board of Trade would like to see any decision intended to reduce the tax burden also take into account the weight of the debt and its impact, in the longer term, on this very same tax burden. It is especially important that future generations not be required to assume the costs of immediate tax cuts.

II. Specific recommendations

In this section, the Board of Trade presents concrete proposals aimed at more effectively responding to the budget principles and expectations presented in the Section I. These recommendations revolve around two main themes: improving city financing, and boosting Canada's innovativeness, productivity and economic competitiveness.

1. Improving city financing

Several organizations,[1] including the Board of Trade, have noticed in the past few years that Canadian municipalities lack sufficient revenues to adequately fulfill their increasingly diverse responsibilities and that they are overly dependent on property tax revenues. In the last decade, not only have municipal revenues advanced at a slower pace than those of the upper levels of government (provincial and federal), their responsibilities have expanded considerably, and their revenues were not always adjusted accordingly. For example, between 1995 and 2001, while the Canadian economy grew 31%, federal and provincial revenues advanced 38% and 30% respectively. During the same period, municipal revenues increased only 14%.[2]

The small revenue growth of municipalities, combined with their inability to diversify their income sources, have placed them in a particularly difficult situation. Following various municipal reforms in Quebec during the 1990s, over $1.1 billion in new responsibilities were transferred to the municipalities[3] (mass transit, social housing, recreation, environmental standards, water quality, etc.). The municipalities of Quebec and Canada have therefore directly and substantially helped the upper levels of government achieve a zero deficit – so much so that according to the Organization for Economic Cooperation and Development (OECD) and the president of the Conference Board of Canada,[4] it is Canadian cities rather than the provincial governments that are truly feeling the effects of the "fiscal imbalance."

Urban infrastructures are being especially hard hit by this financial context. Faced with a budgetary impasse, the municipalities prefer to indefinitely postpone investment in their aging infrastructures rather than slash services to citizens – what the Conference Board of Canada refers to as the "hidden deficit." For the City of Montreal, the value of investments to rehabilitate urban infrastructures (water management, road repair, bringing real estate properties up to standard, mass transit) is estimated at $5.9 billion.[5] This figure does not include new construction but only what is required to upgrade existing infrastructures after 15 years of forced neglect.

For the Board of Trade, all these elements raise major concerns. On the one hand, the health of urban infrastructures, as pointed out in a study published by Statistics Canada,[6] is a major factor that can affect the operating and production costs of businesses and merchants, particularly in terms of merchandise flow and transportation. On the other hand, these same businesses and merchants, through business taxes and property tax on non-residential properties, are among the largest contributors to city financing. In the case of Montreal, property tax on non-residential properties for the 2004 budget equals 41% of

---

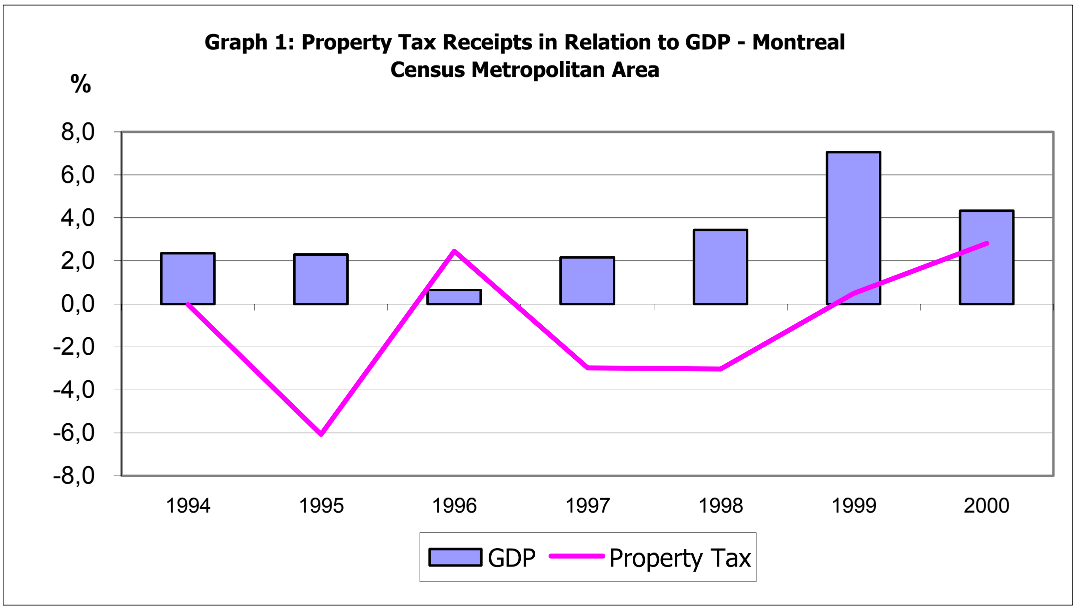
[1] Among others, the TD Bank, Conference Board of Canada, Federation of Canadian Municipalities, Round Table on Environment and the Economy, and the Union des Municipalités du Québec.
[2] TD Bank Financial Group, *A Choice between Investing in Canada's Cities or Disinvesting in Canada's Future* (2002).
[3] Conference Board of Canada and the Union des Municipalités du Québec: *La situation fiscale des municipalités québécoises*, May 2003.
[4] URBA, publication of the Union des Municipalités du Québec, vol. 24 no. 2, April 2004.
[5] Presentation by Frank Zampino, President of the Executive Committee of the City of Montreal, to the Board of Trade, October 2002.
[6] Harchaoui, Tarek M. and Faoui Tarkhani, *Public Infrastructure in Canada*, Statistics Canada, November 2003.

the taxes collected by the City – whereas this category of property represents only 28% of the taxable property value. In light of its numerous responsibilities and the weight of its commitments – notably, the actuarial deficit – Montreal can only reinvest a small portion of the revenues drawn from economic activity in the City's growth, for example, through core projects or additional infrastructure investments. For the Board of Trade, this raises the question of whether this way of doing things does not in the long term hinder the growth of the Montreal economy, and in so doing, limit the natural growth of the City's revenues.

Rethink, increase and diversify

The over-dependence of cities on property tax revenues is the main reason for their financial difficulties. In 2004, 73.7% of Montreal's revenues will come from properties – property taxes, taxes aimed at non-residential property owners and compensation in lieu of taxes. Elsewhere in Quebec, the average proportion is 76%.

The property tax is poorly adapted to the new and ever expanding municipal responsibilities: It is a tax base that does not evolve at the same rate as economic growth and is a regressive form of taxation (the proportion of personal income allocated to paying property tax drops as personal income increases). From 1994 to 2000, property tax receipts rose an average of 0.38% while the province's GDP grew 2.89% annually. This situation is all the more pronounced in cities of the Montreal census metropolitan area, where property tax revenues dropped 0.96% on average while regional GDP expanded 3.18%. Graph 1 clearly shows this inequity in Montreal.



Source: Conference Board of Canada and Union des municipalités du Québec.

A jump in property values – as has just taken place in Montreal – does not necessarily solve the problem. Based on market conditions in Montreal on July 1, 2002, the value of 411,550 residential and non-residential properties on the City's new valuation roll rose 22.7% on average over 2000. Unfortunately, this is only an increase "on paper." In fact, for the owners of these properties, the increase in their personal wealth remains theoretical: they do not necessarily have more money in their pockets. As such, the City cannot hope to see its revenues advance by the same proportion without radically increasing the burden of its taxpayers.

For the Board of Trade, it is therefore imperative that the Canadian government work closely with the provincial governments and representatives of Canadian cities to find ways to boost and diversify city revenue sources.

The reflection in this regard should begin this fiscal year and lead to profound, lasting changes in city financing by no later than the 2005-2006 budget. The solutions should provide for new, increased, diversified and predictable revenue sources. In this regard, the exercise conducted by the City of Winnipeg and its mayor, Glenn Murray, to rethink the city's revenue sources should inspire similar exercises elsewhere in the country.[7] Although there is no one solution to the problem of city financing; the objectives pursued by the City of Winnipeg are common to all urban centres in the country: 1) rebuild and maintain infrastructures; 2) create a tax system that rewards investment, promotes environmental values and makes taxation more equitable; and 3) enrich the city's culture, social and economic life.

Needless to say, the Board of Trade is not making this recommendation merely to see more public funds flow to municipalities for day-to-day operations. The Board of Trade is concerned about the rising cost of public services provided by Greater Montreal's cities and expects municipal administrations to make continuous efforts to reduce expenses. The reason it would like to see new, increased, diversified and predictable revenue sources for the municipalities is because there are needs, notably, in the area of urban infrastructures, and these needs are best addressed by the cities directly concerned.

Recommendation:
That the Government of Canada work closely with the provincial governments and representatives of Canadian cities to find ways of increasing and diversifying the revenue sources of cities. The reflection in this regard should begin during this fiscal year and lead to profound, lasting changes in city financing by no later than the 2005-2006 budget.

While the Board of Trade would very much like to see profound, lasting changes in city financing, it also recognizes the need, in the short term, for new, predictable, recurring and diversified revenue sources. To this end, the Board of Trade proposes a series of measures that complement the previous recommendation and that in addition to meeting the need for increased financial resources can be implemented fairly rapidly. Needless to say, these proposals must not be viewed as individual, stand-alone solutions but rather as complementary approaches that can be implemented without increasing the burden of taxpayers in the Greater Montreal area.

1.1. Transfer a portion of the revenues of the gasoline excise tax

Setting up a mechanism to share a part of the gasoline excise tax as a way of diversifying city revenues is particularly appealing to the Board of Trade and was recommended by the new Prime Minister of Canada, the Right Honourable Paul Martin, on September 25, 2003, during a speech before the Union of British Columbia Municipalities.

The Board of Trade is pleased to see this commitment because it shows that the Canadian government recognizes the importance of urban centres for the economic vitality of the country. Since a direct correlation exists between the growth of cities and the growth of federal revenues, it is only fair and legitimate that the cities have access to a part of this growth. As such, the Board of Trade expects the governments of Quebec and the other provinces to work with the Canadian government to implement this important measure as quickly as possible.

[7] In this regard, see the article signed by Mayor Glenn Murray in the *Chart of December* 2003. Available online at www.btmm.qc.ca

Total receipts for the federal gasoline excise tax amounted to just over $4.5 billion for 2002-2003.[8] Under a scenario that would see 5 cents per litre transferred to the cities, total municipal revenues would increase by $2.25 billion per year.

Needless to say, an equitable way of redistributing these revenues would have to be found so as to avoid a situation in which outlying cities, where more people have and use a car, have an advantage over the central cities where mass transit ridership is proportionately higher. An interesting possibility could be to develop a formula whereby municipalities that make up a given urban area share the revenues generated in that area according to the size of their population and economic activity (measured by GDP). In the case of metropolitan Montreal,[9] it is estimated that under such a scenario, the annual transfer to its municipalities would amount to $154.5 million.

The Board of Trade believes that an important characteristic of such a revenue transfer is permanency. To ensure that cities do not become financially vulnerable to the changing political whims of the Canadian government, this transfer must come with long-term guarantees.

This source of revenue would have to change over time as gasoline consumption habits evolve, notably, in light of the Kyoto Accord: Because Canadian cities should encourage a decrease in gasoline consumption, they will be placed in a situation where if they succeed, they will end up with less revenues. As mentioned earlier, this measure can therefore not be the only solution to the problem of municipal financing and does not eliminate the need to completely rethink city financing.

True to its pragmatic approach, the Board of Trade believes that the financial vice gripping the manoeuvrability of cities makes it especially urgent to find new sources of revenue. Because they have benefited from the contribution of the major cities as economic engines and generators of new revenues, the Board of Trade considers it just, equitable and in the interest of *both* levels of government to develop, in good faith, a mechanism that would give the cities access to some of the revenues generated by the gasoline excise tax while ensuring that their areas of responsibility do not overlap.

Recommendation:
That the Government of Canada share a portion of the gasoline excise tax revenues with the large cities in the country.

1.2. Total reimbursement of the GST

As the Board of Trade stated in its pre-budget submission last year, the status of the municipal administrations vis-à-vis the goods and services tax (GST) is both unusual and surprising. The upper levels of government cannot charge each other sales tax; in fact, they are exempt, thus reducing the cost of the goods and services purchased for their operations and for the delivery of services to citizens, merchants and businesses. For the Board of Trade, the same logic should apply between the federal and provincial governments and the municipalities.

Because they pay GST on every purchase, municipalities currently pay a tax of 7 %. Yet since the vast majority of the goods and services they purchase are used to provide citizens, merchants and businesses with services on which GST is not charged, the cities, rather than the consumer, end up assuming the tax burden at the time of purchase, a situation that runs totally counter to the spirit of the tax.

---

[8] Government of Canada, *Public Accounts of Canada 2003, Volume II, Part I. Details of expenses and revenues*, p. 1.3.

[9] In this specific case, Montreal corresponds to the territory of the Agence métropolitaine de transport, i.e., the 63 communities of the metropolitan Montreal community as well as the Kahnawake Reserve.

To ensure that the municipalities do not assume the full weight of the GST, the government gives them a partial refund of 57.14% of the GST paid. This means they pay a net tax of some 3%, a payment that can be considered an over-contribution to the Government of Canada: 3% consisting of the tax contributions of Montreal citizens, merchants and businesses, that should be used to make purchases necessary for the delivery of municipal services end up in Ottawa's coffers – coffers that these very same citizens, merchants and businesses already help fill through income tax and GST levies on purchases.

Thus, exempting municipalities from the GST or refunding them in full would be in keeping with the spirit of this pact while making it more equitable and significantly reducing the real cost of municipal investment. Canadian municipalities contribute some $465 million in GST payments to the Canadian government every year.[10] In 2002, the City of Montreal paid $70 million in GST and received a refund of $40 million. There is no doubt that fully refunding the GST would greatly improve the financial means of the municipalities of the Montreal region.

Recommendation:
That as of the next budget year, the Government of Canada exempt municipalities from GST or fully refund them the tax.

1.3. Compensation in lieu of taxes

Property tax, based on property assessments, has for some time been the method of choice of municipalities to finance the services they deliver to their citizens, merchants and businesses. In this respect, the Government of Canada, unlike private owners, has enjoyed a special status whereby it does not have to pay the full amount of property taxes, and as a result, the full cost of the municipal services its properties nevertheless enjoy. Even if the Quebec government is required to pay the rates and service charges incurred for services consumed directly by its public buildings, in most cases, these charges are not enough to cover the entire cost of the municipal services. Compensation intended to address this shortfall is referred to as compensation in lieu of taxes.

In 1998, according to the report of Quebec's *Commission nationale sur les finances et la fiscalité locales*, the Canadian government paid Quebec municipalities some $104 million in compensation in lieu of taxes, the equivalent of 73% of the property tax it would have paid on the basis of a property assessment.

The compensation in lieu of taxes paid by the federal government does not equal 100% of the value of the property tax for two reasons: first, because they are set based on accepted value rather than on the rental taxes (business tax for example). In 2004, the compensation in lieu of taxes that the Canadian government and its corporations will pay the City of Montreal will amount to $49 million, including $19 million of compensations for the buildings located on Dorval Airport territory. In addition to these compensations, there are the fees normally paid by Crown corporations that administer their own buildings, namely, Via Rail, Canada Mortgage and Housing Corporation, Canada Post, the Canadian Broadcasting Corporation and the Montreal Port. It is interesting to note that the last two corporations are currently in litigation with the City of Montreal, and arrears dating from 1999 could reach $5 million in each case.

Just as it did for the previous budget year (2003-2004), the Board of Trade is formulating a specific recommendation concerning compensations in lieu of taxes. In the interest of tax equity, the Board of Trade of Metropolitan Montreal supports the conclusion of the *Commission nationale sur les finances et la fiscalité locales* recommending that the Canadian government pay compensations in lieu of taxes equal to

[10] Federation of Canadian Municipalities, *Brief to the House of Commons Standing Committee on Finance,* September 2003.

100% of the local taxes on the property values of its own buildings. Such a measure would simplify the compensations in lieu of taxes plan and increase municipal revenues.

Recommendation:
That the compensation in lieu of taxes paid by the Government of Canada and its Crown corporations to the municipalities equal 100% of the local taxes on the property value of all the buildings they own, as of the next budget year.

2. Enhancing our economic competitiveness

For the Board of Trade, innovation and productivity are the keys to improving the economic competitiveness of Greater Montreal and its businesses. To this end, the measures presented in this section seek to improve either of these factors so as to make the economy of Montreal – and by extension, Quebec and Canada – more competitive.

2.1. Developing creative partnerships to finance urban infrastructures

As stated earlier, municipalities require tremendous financial resources to maintain and renew their urban infrastructures. The City of Montreal alone needs $5.9 billion to rehabilitate its infrastructures. For the Board of Trade, the sustainable economic development of Canada's urban centres hinges on an adequate and rapid response to these needs. First and foremost, efficient infrastructures reduce costs for the businesses and companies that rely on them.[11] For example, one need only think of the cost associated with traffic congestion in the Greater Montreal area, estimated at $600 million per year by former Minister of Transport David Collenette.[12]

Moreover, infrastructure needs are a major burden on municipal administrations and even a threat to their financial equilibrium. In the medium term, the Board of Trade fears that cities will have no choice but to substantially hike taxes or significantly reduce services to citizens, merchants and businesses. Lastly, it is important to remember that adequate, efficient infrastructures contribute to the quality and environment of the city, which in turn, adds to its competitiveness in terms of attracting investors and workers.

While it insists on the importance of immediately meeting the challenge of renewing the urban infrastructures of Canada's urban centres, the Board of Trade understands that it is difficult to finance major investments at a time when health care and education expenses are taking up a growing part of the public purse. In this context, the Board of Trade believes the time has come to innovate and implement new ways of financing urban infrastructures, beginning with close collaboration between all the levels of government – federal, provincial and municipal – and the private sector.

"Public works, private capital" partnerships

Given the high volatility of the stock markets these past few years, financial vehicles offering greater security such as bonds and blue chip stocks have grown in popularity. However, it appears that the

[11] According to a study published by Statistics Canada (Harchaoui, Tarek M. and Faouzi Tarkhani, *Public Capital and Its Contribution to the Productivity Performance of the Canadian Business Sector,* November 2003), the injection of public capital in transportation and mass transit infrastructures, and water distribution and waste water systems saves companies (all sectors combined) 17 cents **per year** for each dollar of public capital invested.
[12] Notes for a speech by Transport Minister David Collenette: *Gridlock: An Economic Deterrent – Solutions for Tomorrow,* Toronto, March 1, 2001.

supply of safe investment vehicles is barely enough to meet demand, creating a ripe opportunity to take advantage of available private capital to carry out public infrastructure projects.

For this reason, the Board of Trade is inviting the three levels of government to examine the avenue of "public works, private capital" partnerships to execute value-added infrastructure projects. The Board of Trade drew its inspiration for this recommendation from the model used in Portland, Oregon, where since the end of the 1950s, numerous housing and neighbourhood revitalization projects, as well as subsidy programs for new or expanding businesses, have seen the light of day.[13] The capital required for these projects is raised by the Portland Development Commission through the sale of bonds. Depending on the nature of the project, the expansion of the tax base (through the higher property values of the properties affected or built as part of the project) is used to repay the principal and interest of the bonds.

Besides making large-scale projects financially possible, this approach is all the more interesting because it cannot be successfully implemented without the involvement of its public and private partners and beneficiaries. Moreover, in order to be approved, the investment must have demonstrable and measurable added value that will make it possible to repay the bondholders.

Under this model, the government's contribution can take various forms: in addition to acting as project developers and implementers, they can also guarantee the bonds issued, making them even more safe, and by extension, less costly.

This way of doing things could be applied with great success to integrated urban development projects similar to the Quartier international or to Société du Havre's development project for the Havre de Montréal. Indeed, in the case of the land use or revitalization project for which private investments are planned, it is in fact possible to forecast the added property value at the end of the project and to finance the infrastructure work required based on anticipated new tax revenues.

By taking this approach, the costs for the different levels of government are relatively small: the upper levels bear the financial risk associated with guaranteeing the bonds while the municipal administration must, for the period of time required to repay the bonds, give up using the additional tax revenues generated by the project to finance their day-to-day operations.

Recommendation:
That the governments of Quebec and Canada, in conjunction with municipal administrations, jointly and actively participate in setting up "public works, private capital" partnerships to finance value-added urban infrastructures.

2.2. Federal capital tax

Aimed at large corporations and financial institutions, Federal capital tax, or large corporations tax, is levied on equity capital, debt capital and capital reserves. Capital is a mobile production factor that can be rapidly moved to those locations that offer the best conditions for profitability. Consequently, investments opportunities in Canada are rendered less attractive to foreign investors, who compare the business tax environments between countries and provinces.

Because it constitutes an additional fixed expense for businesses, capital tax stifles investment and labour productivity. It is also recognized in the business community that this additional expense dissuades innovation and the acquisitions of new technology. This tax imposes a disproportionate burden on highly

[13] For more information in this regard, visit www.pdc.us

capitalized companies such as those operating in manufacturing, natural resources, financial and high-tech sectors, which are strongly concentrated in urban centres. Lastly, this tax is levied without any regards to profitability and can therefore destabilize companies during periods of low earnings or losses.

Capital Tax Rate in 2003			
Canada*	0.225%	**Nunavut**	N/A
Alberta	N/A	**Ontario**	0.30%
British Columbia	N/A	**Quebec**	0.60%
Prince Edward Island	N/A	**Saskatchewan**	0.60%
Manitoba	0.30%	**Newfoundland**	N/A
New Brunswick	0.30%	**Northwest Territories**	N/A
Nova Scotia**	0.25%	**Yukon**	N/A

Source: Samson Bélair Deloitte & Touche

**Earlier in 2003, the Government of Canada announced its plan to abolish the capital tax in 2008.*

***Nova Scotia will no longer charge capital tax as of 2005.*

As for financial institutions (deposit-taking institutions, insurers, etc.), the impact of the capital tax is also significant since it imposes an onerous tax burden. As stated in the report of the Task Force on the Future of the Canadian Financial Services Sector, "Capital taxes render regulated financial institutions less competitive and create incentives that are inconsistent with sound prudential management."[14]

The Board of Trade was pleased to hear the federal government announce in February 2003 that it would abolish the large corporations tax over a five-year period. While one quarter of the companies subject to this tax will no longer be required to pay it as of 2004, for the remainder, this tax continues to discourage investments, hurt competitiveness and productivity, and by extension, job creation. The Board of Trade therefore encourages the government to do whatever is necessary for Canada to quickly catch up to the other OECD nations, which apart from Germany and Japan, have already abolished this type of tax. As well, at a time when the Canadian dollar is appreciating in relation to the greenback and diminishing the competitiveness of Canadian exports, the immediate elimination of the federal capital tax would encourage corporate investments that would boost productivity.

Lastly, the increase in local and foreign investments that would result from the elimination of the capital tax would help increase GDP and in the medium term contribute to compensating the government for the loss of revenues currently derived from the capital tax. The large corporations tax provided the federal government with annual revenues of $1.4 billion in 1999, while the contributions of financial institutions amounted to $143 million.[15]

Recommendation:
That the Government of Canada immediately and completely abolish the large corporations tax, or federal capital tax, a tax measure considered to be highly detrimental to business productivity.

2.3. Measures to support exports

The Greater Montreal area has over 5,000 exporting companies and is home to 70% of all Quebec exporters. The vitality of the export sector plays a major role in the economic growth of Canada.

[14] Task Force on the Future of the Canadian Financial Services Sector, *Change, challenge and opportunities. Report of the Task Force, September* 1998, p. 116.
[15] Conference Board of Canada, *The Case Against Capital Taxes*, 2001.

However, in the past few years a negative trend has emerged in this industry. Economic uncertainties – namely and until just recently, the sluggish economic recovery in the U.S. – and geopolitical uncertainties, as well as weak global economic growth have had a negative impact on our foreign trade.

In fact, data published by Export Development Canada (EDC) reported a 2.6% decrease in the volume of Canadian exports of goods and services in 2002. The outlook is somewhat better for 2003: EDC is forecasting zero growth. Exports thus appear to be on the way to recovery and should grow in 2004, as much as 4% according to EDC. As such, Canadian exports should gain lost ground over the next few months.

Still, the rapid, on-going rise of the Canadian dollar since early 2003 – an increase of 22% in a year[16] – has inevitably complicated the task for Canadian exporters, making our goods and services more expensive for American buyers. Until just recently, sluggish sales in the U.S. negatively impacted the growth of Canadian SMEs. It is important to qualify these concerns because, while our economy, and chiefly our exports are affected by foreign exchange fluctuations, it is the productivity of the domestic economy that truly affects a company's export capacity. Nonetheless, the meteoric rise of the loony is such that Canadian companies have suddenly become less competitive and must act quickly to redress the situation.

Due to their importance, innovative means must be found to support the export activities of Canadian companies and thus contribute to economic growth. This support is all the more essential because, generally speaking, new market developments require major investments and efforts before producing results, and exporters are especially vulnerable to foreign market and currency fluctuations.

In this matter, the Board of Trade considers it pertinent to reiterate its call, launched as part of its 2003-2004 pre-budget submissions, for complementary or joint initiatives on the part of the Quebec and Canadian governments to support export activities.

2.3.1. Government-backed fund

In the current context where the Government of Canada is open to finding innovative ways to help businesses by using private sector resources, the Board of Trade would like to repeat its proposal to set up a government-backed fund devoted exclusively to financing export projects for low- and medium-technology SMEs.

The advantage of such a fund is that it fulfills a real need for a private source of financing for low- and medium-technology companies seeking to develop foreign markets. By guaranteeing a portion (20%, for example) of the potential losses of a private financial institution, the government acts as a facilitator, making available to SMEs as much as five times the financing typically accessible to them. In fact, the first benefit of such a guarantee is that it significantly limits the risk incurred by the financial institution, which should then make financing more accessible and cheaper for small and medium borrowers. The leverage effect of such a fund can be further enhanced by associating an export training and preparation aspect in order to make the companies' foreign market development efforts still more solid and likely to succeed.

Recommendation:
That the Government of Canada set up export support measures such as a government-backed fund devoted exclusively to financing the export projects of low- and medium-technology companies.

[16] For example, a similar increase took 3½ years to materialize at the end of the 1980s.

Conclusion

In the current economic context, the competitiveness – defined as the ability to confront competition on the markets – of economies, industrial sectors and companies is the cornerstone of a society's ability to create wealth for its citizens and an essential condition for improving their quality of life. A number of factors directly or indirectly affect the level of competitiveness. However, economic analysts agree on two key factors: the ability to innovate and the level of productivity, which feed each other. Compared to the United States, Canada lags behind with respect to both these key factors. Such is also the case when Quebec is compared with its main competitors, Ontario and the New England states. Faced with this reality, the budget choices the government is about to make must make it possible to find answers to the challenges of innovation, productivity and competitiveness.

It is with this in mind that the Board of Trade not only presented the expectations of its some 7,000 members with respect to the upcoming budget in this submission, but also put forth constructive proposals likely to improve the economic performance of the Greater Montreal area, and by extension, that of Quebec and Canada. As well, in this same constructive spirit, the Board of Trade would like to impress upon the government that it is available to work together on concrete, fundamental measures that will help grow the Montreal economy.